

No. 12639

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

COMMISSIONER OF INTERNAL REVENUE,

Petitioner,

vs.

BIRCH RANCH AND OIL COMPANY,

Respondent.

ON PETITION FOR REVIEW OF THE DECISION OF THE
TAX COURT OF THE UNITED STATES.

BRIEF FOR THE RESPONDENT.

GEORGE ACRET,

650 South Grand Avenue, Los Angeles 17,

Attorney for Respondent.

FILED

DEC 1 1950

PAUL P. O'BRIEN,

CLERK

TOPICAL INDEX

	PAGE
The opinion below.....	1
Jurisdiction	1
Question presented	1
Statute and Regulations.....	2
Statement of the case.....	3
Argument	20
Point One. The Tax Court did not err in holding that the payments involved are deductible for the reason that under the facts of this case such payments were bona fide payments of taxes assessed against local benefits made for the purpose of meeting interest charges with respect to such benefits	20
A. The \$221,610.87 paid by taxpayer constituted taxes assessed against local benefits.....	23
B. The \$221,610.87 is deductible because it is not "interest paid" but "taxes paid" to meet interest charges with respect to assessments against local benefits.....	29
C. The taxpayer's deduction of the payment of \$221,610.87 as taxes is not in conflict with the purpose of Section 122(d)(2) for the reason that such payment was for taxes actually due and payable, and which in fact did constitute an economic loss.....	31
Point Two. The Reclamation District being regularly formed by a group of eight property owners in addition to the Birches, and the bonds having been regularly issued to pay for improvements of a bona fide value in excess of \$2,000,-000, such District and such bonds did not lose their bona fide character by reason of the subsequent acquisition by respondent corporation, as the Birches' successor in interest, of practically all of the land in the District and a substantial portion of the bonds.....	33

Point Three. Where respondent's predecessor in interest, Mr. Birch, was nearly seventy years old and during the depression could not get bank credit sufficient to enable him to operate the ranch unless he placed the title thereof in a corporation, and where the taxpayer corporation was formed for the purpose of securing such bank credit, there is no question of alter ego, and the corporation is an entirely separate legal entity with respect to taxation, as well as in every other respect..... 34

Conclusion 36

Appendices:

Appendix A. Bond of Reclamation District 2035, United States of America, State of California, County of Yolo.....	
.....App. p.	1
Appendix B. Excerpts from Section 3480 of the California Political Code, with appropriate emphasis added.....App. p.	3

TABLE OF AUTHORITIES CITED.

CASES	PAGE
Andrew v. Little, 21 B. T. A. 911.....	21, 30
Western Insurance Company v. Drainage District 72, 72 Cal. App. 68	25, 27

STATUTES

Political Code, Sec. 3478.....	24
Political Code, Sec. 3480.....	2, 25, 28, 29, 30

No. 12639
IN THE
United States Court of Appeals
FOR THE NINTH CIRCUIT

COMMISSIONER OF INTERNAL REVENUE,

Petitioner,

vs.

BIRCH RANCH AND OIL COMPANY,

Respondent.

BRIEF FOR THE RESPONDENT.

The Opinion Below.

The findings of fact and opinion of the Tax Court are set forth at R. 385-408 and are reported at 13 T. C. 930.

Jurisdiction.

The jurisdiction is as stated in Appellants' Brief.

Question Presented.

The question presented is as set forth in Appellants' Brief and is as follows:

1. "Whether the circumstances of the case are such as to entitle the taxpayer-corporation to a 'taxes paid' deduction under Section 23(c) of the Internal Revenue Code, or to an 'interest paid' deduction under Sections 23(b), 122(a) and (d) (2), in computing its 1944 net operating loss for the purpose of a carry-back deduction in the taxable year 1942 under Sections 23(s) and 122."

It seems to respondent, the following questions are also presented:

2. Where a reclamation district is regularly formed by a group of eight property owners, including the Birches, and where bonds covering the district are regularly issued and nearly one-half thereof is owned by various persons other than Birches and are dealt in for value over a period of nearly twenty years, does such district, and do such bonds, lose their bona fide character by reason of the acquisition by respondent corporation, as the Birches' successor in interest, of practically all of the land in the district, and by reason of the Birches' gradual acquisition of all of such bonds over such period?

3. Where Mr. Birch was nearly 70 years old and during the depression could not get bank credit sufficient to enable him to operate the ranch unless he placed the title thereof in a corporation, and where the taxpayer corporation was formed for the purpose of securing bank credit, is not the corporation a separate legal entity, and does not this fact furnish an additional reason as to why it is entitled to deduct as taxes all assessments paid by it to the County Treasurer covering its lands, irrespective of who owns the bonds?

Statute and Regulations.

The statute and treasury regulations are set forth in the Appendix to Appellants' Brief. Appellant, however, fails to set forth the pertinent portions of the California statute applicable to reclamation districts and the issuance of reclamation bonds. The applicable portions of this statute are set forth in an Appendix to this brief. (Pt. 3, Tit. 8, Ch. 1, Art. 2, Secs. 3478 and 3480.)

Statement of the Case.

Appellants correctly set forth in their brief the Tax Court's findings of fact. [R. 387-397.] The Stipulation of Facts, the exhibits (separately transmitted by stipulation) and the testimony of respondents' witnesses, are also pertinent as additional facts which support the Tax Court's opinion and conclusions of law.

The Stipulation of Facts appears at R. 134-147. The testimony of respondents' witnesses appears at R. 211-349.

The respondents' exhibits were admitted at the following pages in the record and consist of the following:

Page 197	Exhibit 1—photostatic copy of report of Commissioner with respect to taxpayer.
Page 201	Exhibit 2—findings of fact of Judge Turner in former case.
Page 202	Joint Exhibit 3a—respondents' income tax return for the year ending September 30, 1944.
Page 206	Exhibit 5—judgment roll finding formation of reclamation district 2035 to be sufficient and legal.
Page 206	Exhibit 6—judgment roll finding first bond issue sufficient and legal.
Page 209	Exhibit 7—judgment roll finding re-funding bond issue sufficient and legal.
Page 210	Exhibit 8—copy of cancelled bond No. 2000 of first issue.

Respondents' Exhibits.

- Pages 215-219 Exhibits 9 to 12—calls of County Treasurer with respect to assessments against reclamation district, correspondence relating thereto, and taxpayers' payment as taxes totaling the said sum of \$221,610.87, being the amount referred to in said Exhibit 2 and being the item of deduction involved in the within action.
- Page 274 Joint Exhibit 13f—return for year ending September 30, 1942.
- Page 278 Exhibit 14—first Hopkins contract.
- Page 279 Exhibit 15—second Hopkins contract.

Appellants' Exhibits.

- Page 228 Exhibit B—letter produced by Mr. Landrum regarding payment of assessment.
- Page 230 Exhibit C—correspondence between respondent and County Treasurer.
- Page 232 Exhibit D—ditto.
- Page 234 Exhibit E—letters relating to call No. 23, showing payment of call by means of interest coupons as permitted by statute.

The findings of fact of the Tax Court taken as a whole, and the aforesaid evidence and stipulation would seem to impel the following conclusions: (1) reclamation district 2035 is a bona fide reclamation district and state agency and a separate legal entity, entirely distinct from

the land owner within the district; (2) the \$2,000,000 reclamation bonds were regularly issued and are valid and existing bonds, the principal of which, together with its interest thereon, constitutes a lien against all lands of the district until paid; (3) respondents' payments to the County Treasurer, or its purchase of the interest coupons and the bonds and the delivery of such to the County Treasurer, under the Reclamation Act constituted payment of taxes and not interest; (4) and that respondent is not economically identical with the district or the bonds.

In its opinion the trial court stated in part as follows:

“The essential factual premises or inferences which respondent assumes for this argument are not adequately supported by the evidence.” [R. 403.]

For the reason that respondent has disregarded essential and material facts of the case, it will be helpful if we quote here from a portion of the partial stipulation of facts, with appropriate emphasis added, as follows:

“6. Desiring to reclaim and develop the lands comprising the Conaway Ranch, the Birch Oil Company, in 1918, filed a petition with the Board of Supervisors of Yolo County, California, for the creation of a reclamation district which would include 24,210 acres and would cover the whole of the Conaway Ranch and twenty-odd other parcels of land not owned by the Birch Oil Company or its members. In April 1919, the establishment of Reclamation District No. 2035, comprising approximately 21,000 acres, was approved by the Board of Supervisors. *Excluded from the district as approved were some 1,300 acres of the Conaway Ranch and all except eight of the twenty-odd other parcels of land not owned by the Birch Oil Company or its members.*” [R. 136.]

“7. Organization of the district was completed and the County Board of Supervisors appointed Conway, C. Harold Hopkins, and a man named Armfield as trustees for the district. In June 1919, the trustees employed an engineer and directed him to prepare plans for the reclamation and irrigation of lands in the district, with estimates of the cost of the necessary improvements. In June, 1920, the trustees approved the plans submitted by the engineer and his estimate of \$2,264,740 as the cost of the improvements. The plans submitted called for the construction of the main levee along the edge of the Yolo By-pass, as above described. The plans were approved by the Reclamation Board of the State of California in October 1920, and in December of the same year, by the Board of Supervisors. Commissioners of assessment were appointed to assess the value of the benefits to the lands in the district from the improvements contemplated and to apportion the cost of said improvements according to the benefits that would accrue to each tract of land in the district. Thereafter, and prior to July 2, 1924, the commissioners made the assessment and apportionment for which they were appointed. The assessment was approved by the Board of Supervisors on July 23, 1924; and the list of assessment was filed on the same day with the County Treasurer of Yolo County.” [R. 137.]

“8. The Birch Oil Company, under the direction of the district's engineer, built the improvements called for in the reclamation plan and financed all the costs, which were slightly in excess of two million dollars. The work was substantially completed by 1925, at which time the improvements consisted of 45 miles of roadways, 47 miles of irrigation canals, 55 miles of drainage canals and ditches, and included

bridges, pumping plants and other structures necessary for the development of the lands in the district. By 1925 Birch had acquired individually and at undisclosed costs seven of the eight parcels of land which with the Conaway Ranch comprised the land of the district. The parcel not so purchased consisted of 240 acres." [R. 138.]

"9. In the meantime, the Hopkins sisters, being desirous of disposing of their interests in the Conaway Ranch, by agreements dated January 1, 1924, sold such interests to Birch and Mrs. Birch for \$787,000, an amount designed to pay them their proportionate part of the Birch Oil Company funds invested in the ranch. Under the agreements each of the sisters agreed to accept bonds of Reclamation District No. 2035 in the principal amount of \$393,000 and cash in the sum of \$500. Birch and his wife agreed to cause the district to issue bonds in an amount of at least \$800,000, which were to constitute a prior lien on all of the property in the district, and further promised to deliver on or before February 1, 1925, to each of the sisters the amount of the bonds and cash called for by the agreements. Birch and his wife were to have immediate and absolute possession and control of the properties acquired from the Hopkins sisters and were to be entitled to all rents and profits of every kind therefrom and were to assume all liabilities and burdens incident to the ownership thereof. The bonds not having been issued at the time of the agreements of January 1, 1924, Birch gave to each of the sisters his promissory note in an amount equal to the amount of the bonds she was entitled to receive under the agreements. The notes were to run for 10 years and were to draw interest at 6 per cent per annum from January 1, 1924, for

a period of 5 years, and at 7 per cent thereafter. Birch had the option of paying the notes in full at any time prior to the expiration of the 10 year period." [R. 139.]

"10. According to the minutes, the landowners, at an election held on August 28, 1924, voted to issue bonds to pay for the reclamation work which had been done, and on October 26, 1924, the trustees adopted resolutions providing for the issuance of the bonds." [R. 139.]

"11. On January 5, 1925, the trustees of the district adopted resolutions directing that the district pay Birch and Conaway \$2,000,000 for moneys advanced in the construction of the improvements; that Warrant No. 1 of the district be issued to them in that amount; that the bonds of the district be placed in the hands of the County Treasurer; and that the County Treasurer be requested to advertise the bonds for sale at the earliest possible date. On the same day Warrant No. 1 for \$2,000,000, drawn on the Treasurer of Yolo County, was issued to Conaway and Birch. The warrant was approved by the Board of Supervisors of Yolo County and was presented for payment to the County Treasurer but was not paid for want of funds." [R. 139.]

"12. On January 7, 1925, the trustees of the district delivered to the County Treasurer bonds of the district totaling \$2,264,740. The bonds were dated January 1, 1925, and bore interest at the rate of 6 per cent per annum until paid. They were in denominations of \$1,000. The first \$227,000 thereof were to mature on January 1, 1935, with a like amount maturing on January 1 of each year following until January 1, 1944, when the bonds then remaining and amounting to \$221,740, were to mature. Also on

January 7, 1925, the County Treasurer gave notice that on January 23, 1925, he would sell Bonds Nos. 1 to 2,000, inclusive, of \$2,000,000 par value, to the highest bidder, and stated that outstanding warrants of the district, with accrued interest thereon, would be accepted in payment for the bonds. Birch, acting for himself, Mrs. Birch and the Conaways, was the highest bidder, his bid being \$2,000,000 plus accrued interest. Being the highest bidder, he became the purchaser of the bonds and gave in payment therefor Warrant No. 1 of the district, which had been received by him and Conaway in payment for the building of the improvements for the district." [R. 140.]

"13. Upon receipt of the bonds of the district, Birch delivered to each of the Hopkins sisters \$393,000 par value of such bonds, or a total of \$786,000, pursuant to the agreements of January 1, 1924, whereunder he and his wife had acquired from the Hopkins sisters all of the interests of the latter in the Conaway Ranch. Upon delivery of the bonds, the Hopkins sisters delivered to Birch the promissory notes covering the purchase price of their interests in the ranch which had been received from him at the time of the January 1, 1924 agreements. At the same time they made formal conveyance to Birch and his wife of all their interests in the Conaway Ranch." [R. 140.]

"14. At or about the same time and pursuant to the terms of agreements dated January 10, 1925, the Hopkins sisters granted to Birch and his wife the right to purchase the bonds received by them as above set forth, at the prices and on the terms set forth in the said agreements. According to these agreements, Birch and his wife offered and agreed to purchase at face the bonds in question, the purchases

from each sister to be made in installments of \$39,300 on January 1, 1926, and on January 1 of each year thereafter until January 1, 1933, with a final installment of \$78,600 on January 1, 1934, and on each purchase date to buy all matured coupons appertaining to the bonds covered in the particular installment. At each installment date the sale of the bonds by the Hopkins sisters to Birch and his wife was to be completed at the option of the Hopkins sisters. To assure payment for the respective installments of the bonds, Birch and his wife agreed to deliver to B. F. Conaway and C. Harold Hopkins, as trustees, the balance of the district's outstanding bonds in the amount of \$1,214,000, and upon default in the payment of any of the above installments, the Hopkins sisters were to be permitted to sell, or have sold, so much of the bonds held in trust as should be required to pay the amount in default. The trustees might also release to Birch and his wife such of the bonds as might be required by them as a pledge for money borrowed to pay any current installment. Otherwise the bonds held in trust were to be released by the trustees only upon the written consent of the Hopkins sisters or upon full performance of the agreements by Birch and his wife. In the event the Hopkins sisters should elect at any installment date not to sell the bonds called for by the agreements, Birch and his wife had the option to declare the agreement at an end. Provision was also made that Birch and his wife, on 90 days notice, might elect to buy bonds in advance of the regular installment dates provided and similarly might declare the entire agreement at an end if the Hopkins sisters should reject the offer. In respect of all purchases prior to January 1, 1929, Birch and his wife were to pay interest at the rate of six per cent, the rate called for by bonds. On pur-

chases after that date, they were obligated to pay seven per cent or one per cent over the interest provided for in the bonds.” [R. 142.]

“15. In 1926 Birch entered into an agreement with the Conaways for the purchase of their interests in the ranch and in the bonds of Reclamation District No. 2035. The purchase price was paid in cash and in installments.” [R. 142.]

“16. Beginning with January 1, 1926, the first installment date under the agreements of January 10, 1925, the Hopkins sisters elected to sell the bonds to Birch and his wife pursuant to the terms of the said agreements. Birch and his wife made the payments on the bond purchases as called for in the agreements and as elected by the Hopkins sisters until the early 1930's, when, due to the depression and a resulting lack of funds, they were unable to make the further payments on the dates prescribed, and extensions of time have thereafter been allowed. The bonds paid for in the face amount of \$476,000 were delivered to Birch and his wife. The Hopkins sisters, in April, 1943,* still held the remaining \$310,000 of the said bonds, but still held Birch and his wife liable on their obligations under the agreements of January 10, 1925. Their interest is in the receipt of the cash payments provided for in the contracts and they are unwilling to accept anything else. Of the \$476,000 par value of the bonds paid for by Birch and his wife and received from the Hopkins sisters, \$10,000 par value of such bonds were sold to Lulu M. Minter and \$86,000 passed into the hands of the

*On April 5 and 6, 1943, the Tax Court heard the case of *Birch Ranch and Oil Company*, Docket 109993, Memorandum Opinion entered April 20, 1944, which related to the years 1937 and 1939.

Great Republic Life Insurance Company, a corporation of which Birch was president. There was later a dispute between petitioner and the insurance company over rights of petitioner in and to the said bonds, the exact basis for which dispute is not shown." [R. 143.]

"17. On October 15, 1934, Birch and his wife organized Birch Ranch and Oil Company, the petitioner herein, and transferred to it the Conaway Ranch, their interest in the Birch Oil Company, the partnership which succeeded the Menges Oil Company in 1911, and all other property belonging to them, except the bonds of Reclamation District No. 2035, certain corporate stock and other properties having a value of about \$600,000. Birch had been having difficulties during the depression years in borrowing on his personal credit the moneys needed for the operation of the ranch, and *the petitioner was organized for the purpose of procuring needed bank credit.*" [R. 144.]

In his findings of fact in his preceding case, No. 19059 [Exhibit 2 herein] Judge Turner found as follows:

"In a proceeding brought by the trustees to determine the legality of the district, the Superior Court of California in and for the County of Yolo, in June, 1920, entered its judgment that Reclamation District No. 2035 is 'a duly and regularly organized and legal Reclamation District.' " [Exhibit 2, p. 86.]

* * * * *

"In a proceeding brought by the trustees of the district, the Superior Court of California, in and for the County of Yolo, on March 2, 1925, entered its judgment 'that said bonds are a valid legal obligation of said Reclamation District No. 2035.' " [Exhibit 2, p. 89.]

* * * * *

“Beginning in 1925, up to and including 1934, Birch and his wife for the Conaway Ranch formally paid over \$120,000 per year for disbursement as interest on the bonds of Reclamation District No. 2035. Such portion of the amount so paid as was applicable to bonds owned by Birch and his wife was repaid to them, but under a claim that interest on such bonds was tax exempt, the amounts so received were not reported by them as taxable income. In each of the said years, Birch and his wife, on their income tax returns, claimed a deduction of \$120,000 as interest paid. *The propriety of these deductions was questioned by the Bureau of Internal Revenue for practically every year, but in each instance the deduction was ultimately allowed.*”* (Emphasis added.)

“On October 15, 1934, Birch and his wife organized Birch Ranch and Oil Company, the petitioner, herein, and transferred to it the Conaway Ranch, their interest in the Birch Oil Company, the partnership which succeeded the Menges Oil Company in 1911, and all other property belonging to them, except the bonds of Reclamation District No. 2035, certain corporate stock and other properties having a value of about \$600,000. Birch had been having difficulties during the depression years in borrowing on his personal credit the moneys needed for the operation of the ranch, *and the petitioner was organized for the purpose of procuring needed bank credit.*” [Said Exhibit 2, p. 93.] (Emphasis added.)

*This was before the incorporation of the Birch Ranch and Oil Company and the Birch Securities Company and while the Birches owned all the land except 240 acres and all the bonds except those owned by the Hopkins, Miss Minter and the Republic Life.

The Superior Court of Yolo County by a judgment duly rendered determined that the refunding bonds issued in 1935 are a valid legal obligation of said Reclamation District 2035. [Exhibit 7 herein.]

Through respondents' witnesses the following facts were also established:

Over a period of years commencing in 1925 and ending in 1946, the bonds of the entire bond issue were dealt in at their face value as to both principal and interest with one minor exception, with respect to 86 shares. [Stipulation of Facts, *supra*, and R. 262, 267, 276, 277, 280, 285, 306, 309, 314, 315, 317, 318, 319, 321 and 324.]

During the five years following 1920, Mr. and Mrs. Birch acquired seven of the eight parcels of land which were included in the district by the Board of Supervisors and which were not a part of the Conaway ranch. [R. 136.]

At the time of the incorporation of the Birch Ranch and Oil Company, Mr. and Mrs. Birch owned \$1,594,000 of the bonds; the Hopkins, \$310,000; Lulu Minter, \$10,000; and the Great Republic Life Insurance Company, \$86,000. [R. 277.]

The Birch Securities Company finished the purchase of the balance of the Hopkins bonds in March, 1944, at a price equal to the par value of the bonds. [R. 280.]

By 1946 the Birchs had acquired all of the bonds and sold them at par to a Mr. Rasmussen. [R. 316.]

No bonds were ever sold or dealt in at less than par, except the Great Republic Life Insurance Company 86 bonds, which were sold for \$65,000. [R. 276.]

In the stipulation it says: "Beginning with 1937 and until 1943, no amount has been paid in any year by petitioner (respondent herein) as interest on the 1,594,000 of such bonds transferred by Birch and wife to the Birch Securities Company." That statement is incorrect in that "it seems that the common expression is that we pay interest into the County Treasury to pay the interest on the bonds, whereas the proper notation and entry would be that we pay the assessment that is levied by the district to meet the interest on the bonds." [R. 284.]

For the first six years of the Hopkins contract, beginning with 1925, the Hopkins collected the interest on the bonds through their collection from the County Treasury on the coupons that matured on the bonds. Mr. and Mrs. Birch paid the assessment based on the call from the County Treasurer on the bonds. This provided for the interest payment, and the Hopkins cashed their coupons. [R. 285.]

From 1931 to 1934, Mr. and Mrs. Birch purchased the coupons from the Hopkins by paying the face value of the coupons as they matured. They turned the coupons in to the County Treasurer, keeping in mind the provisions of the statute. (Appendix B herein, providing for the interest coupons to be turned in to the County Treasurer in payment of assessments the same as money.)

Exhibit One is the usual form of receipt from the County Treasurer of payment upon either turning in coupons or turning in money. [R. 286.]

When Mr. and Mrs. Birch received back from the County Treasurer interest in their coupons, they did not take that into account as part of their income, as it was exempt income. From 1925 to 1934 while they personally

owned those bonds this procedure was questioned every year by the Commissioner and was never disapproved. [R. 287.]

The reference in the stipulation to the bonds owned by the Birch Ranch and Oil Company and the Great Republic Life Insurance Company not being paid by April, 1936, is incorrect. All assessments were paid up until 1937, but subsequent to that, up to 1943, no payments were made. This was because the company was unable to raise any funds. It did not have the money and could not borrow any. The depression period was still on at that time. The bank that we had our account in at Sacramento failed and tied up our funds. [R. 288.]

All assessments of the Reclamation District were paid during the fiscal year ending September 30, 1944. [R. 290.]

At that time the Birches companies were in a little different financial shape, and were able to take care of the various obligations. [R. 290.]

The stipulation on page 14 reads that: "on its books for the fiscal years 1937 and 1939 the Birch Ranch and Oil Company accrued \$120,000 to represent (interest) on the entire two million par value of issued bonds." That statement is incorrect. [R. 292.]

The company had employed a bookkeeper to open up the corporation books, and he interpreted that payment as a payment of interest, rather than a payment of an assessment, and he treated the payment to the Hopkins as paying them interest on our obligations under the contract, rather than paying the assessment so that the Hopkins could cash the coupons that matured at that time. It was not discovered that it was handled that way until the

question was raised by a field agent of the government. [R. 295.]

In participating as one of the landowners in the formation of the Reclamation District No. 2035, the Birches did not have any intention of tax avoidance. The fact never occurred to them. [R. 297.]

Mr. and Mrs. Birch and Mr. and Mrs. Conaway in performing the contract for the improvements of the Reclamation District spent an amount in excess of \$2,000,000, for which they received the warrant in that amount. [R. 297.] They did not get the bonds until six or seven years later. [R. 298.]

The Birch Ranch and Oil Company was a party to the agreement in selling the ranch and Mr. and Mrs. Birch to the agreement for selling the bonds. [R. 306.]

At the time the Birch Securities Company was incorporated in 1934 it received \$1,594,000.00 in bonds. [R. 309.]

Mr. and Mrs. Birch personally guaranteed Mr. Rasmussen under the option that they would be able to deliver all of the bonds. They were contemplating dissolving the Birch Securities Company, and therefore the bonds would come back to Mr. and Mrs. Birch. By July 1, 1946, the option was exercised. By that time the dissolution of the Birch Securities Company had taken place, and Mr. and Mrs. Birch owned all the bonds. [R. 316.]

By March 15, 1944, the Hopkins agreements were marked "cancelled." By this time the Birches had paid the Hopkins the sum of \$260,000 in cash, which was for the balance of the Hopkins bonds. [R. 321.]

In 1943 there was a large amount of unpaid interest on the bonds, but the County Treasurer was not doing

anything about that, as far as foreclosing on the land was concerned. If they did not make any calls, there wasn't any default. [R. 328.]

The County Treasurers all over the state generally were doing this to help out the land owners. [R. 261.]

Exhibits 9, 10, 11 and 12 relate to calls made by the County Treasurer and payments made by respondent. The first calls were made to cover coupons that had matured. After all past due coupons had been redeemed, then regular calls were made for the current accumulation and maturity of the interest on the bonds. [R. 329.]

The reason payments were made in 1943 and 1944 was not simply because the company's bookkeeping was on a cash basis. The reason was because the company was able to raise the funds to pay them. Prior to that time, during the depression, it could not even pay the county taxes, or the assessments, on the Reclamation District. [R. 331.]

The company did not borrow money to pay an assessment. The loans it got from the bank were for the operation of the ranch, and not for the purpose of paying an assessment. [R. 332.]

At the time of the Rasmussen transaction, all of the coupons were paid, but the bonds had not been paid for in full to the Hopkins. [R. 332.]

All the arrears of the past due coupons were taken up by 1944. [R. 333.]

In June, 1946, there were several payments to the County Treasurer aggregating \$474,272.53. That was closing up everything that was due and past due on the bonds. [R. 333.]

The fact that bonds which are issued are tax exempt, did not enter into reason for the organization of the Reclamation District. [R. 334.]

The reason that the bonds were not paid off and were refunded was that we did not have the funds to pay the bonds and it was a common practice for all districts to refund bonds from time to time. That is provided for in the statute. [R. 335.]

The first bond issue came due in 1935, and we were under quite a depression at that time. The company could not meet the payments, and therefore the only alternative was to have a new bond issue. [R. 335.]

At the time of the organization of the district, Mr. Birch did not receive any advice from any attorney or accountant with respect to the tax phase of the matter. The Birches did not have any thought in mind of ever getting out a bond issue. That matter first came to their attention after they received the bonds in 1925. They did not know of that feature before that time. [R. 338.]

The Hopkins never at any time permitted any of the interest coupons to become past due. All interest coupons on the bonds owned by the Hopkins were purchased by the Birch Ranch and Oil Company as they became due. [R. 262.]

Also the coupons of the bonds owned by Miss Minter. All these coupons were turned into the County Treasury under the provisions of Section 3482, which provides they may be turned in the same as money. [R. 263.]

The coupons were always purchased for the full face value. [R. 267.] Also in every instance except as to the 86 Republic Life bonds the bonds were dealt in at their full face value. [R. 276.]

ARGUMENT.

POINT ONE.

The Tax Court Did Not Err in Holding That the Payments Involved Are Deductible for the Reason That Under the Facts of This Case Such Payments Were Bona Fide Payments of Taxes Assessed Against Local Benefits Made for the Purpose of Meeting Interest Charges With Respect to Such Benefits.

The Tax Court stated in its opinion as follows:

“By section 23(c)(1), Internal Revenue Code, taxes paid or accrued within the taxable year are deductible except:

(E) taxes assessed against local benefits of a kind tending to increase the value of the property assessed; but this paragraph shall not exclude the allowance as a deduction of so much of such taxes as is properly allocable to maintenance or interest charges; * * *

As all of the \$221,610.87 paid to the County Treasurer was for application to interest charges, none of it is excluded as a deduction by the statutory exceptions, and respondent does not contend that it was.”
[R. 400.]

Attention should also be directed to the fact that Treasury Regulations III set forth at page 34 of Appellant's Brief, with respect to deductions similar to those involved here, provide as follows:

“Assessments under the statutes of California relating to irrigation and of Iowa relating to drainage, and under certain statutes of Tennessee relating to

levees, are limited to property benefited, and if the assessments are so limited, the amounts paid thereunder are not deductible as taxes. *The above statements are subject to the exception that in so far as assessments against local benefits are made for the purpose of maintenance or repair or for the purpose of meeting interest charges with respect to such benefits, they are deductible.*”

This rule is recognized by and interpreted in the opinion in the case of *Andrew Little*, 21 B. T. A., 911-915, in which it is held that interest on reclamation bonds is deductible as taxes within the meaning of a similar section which existed as part of the Revenue Act of 1921.

It would seem that the facts stated in the preceding statement of the case and in the stipulation of facts [R. 134-147] uncontrovertibly establish that the assessments which are the basis for the deduction involved herein were made for the purpose of meeting interest charges with respect to local benefits within the provisions of the above-quoted regulations.

In his Opening Brief, appellant claims that the deduction involved herein is not proper because “here the improvements involved were paid at the outset by the only party against whom taxes could otherwise have been levied to pay for the improvements.” He also claims that “the whole arrangement, although authorized by the law of California, was merely one through which the Birches had reclamation district bonds issued for their own purposes in which they used it to create personal indebtedness.” He claims that “there was no assessment for benefits received from the drainage improvements”; (because) “at the time the drainage improvements were made in

1924, the Conaway Ranch was owned by taxpayer's predecessor."

The Statement of Facts heretofore presented established that the facts of the case are contrary to these statements. Appellant's entire argument rests upon the false basis of these incorrect statements. For this reason authorities under each of his points have no application to the facts of the case.

After stating appellants' contentions as to why respondent had no right to deduct the said sum of \$221,610.87 paid to the County Treasurer to meet such interest charges, the Tax Court in its opinion summarized appellant's fallacious reasoning and respondent's right to make such deduction in the following words:

"The essential factual premises or inferences which respondent assumes for this argument are not adequately supported by the evidence. We can disregard as negligible the 240 district acres which petitioner did not own and against which an assessment for bond interest apparently was not made, but we can not lightly ignore a public district invested with taxing powers and other sovereign attributes and the substance attaching to the very large number of bonds which were held by parties who had no identity of interest with the Birches and whose right to bond interest was consistently observed, in one case, after threat of suit. The Hopkins sisters acquired 786 of the 2000 bonds in 1925; they owned 310 from 1931 to March 15, 1944, or during five and a half months of fiscal 1944. At an undisclosed date the Birches sold 86 bonds to the Great Republic Life Insurance Co., and its successor sold these bonds to petitioner in 1940; the Birches sold 10 bonds to Lula Minter who held them throughout fiscal 1944. Peti-

tioner regularly paid to the Hopkins sisters and to Lula Minter the amount of accrued interest due them, receiving and turning over the interest coupons to the County Treasurer. By so doing it acquired a credit in the same amount on the district's assessment for interest. See section 11, article II, chapter 1, Title 8, Part 8, Political Code of California, and hence it is not technically correct to say that no assessment taxes were paid from 1937 to 1944. An amount of \$19,200 was paid each year, and by this Court's decision in Docket No. 109993 the amounts so paid were deductible." [R. 403.] (Emphasis added.)

A. The \$221,610.87 Paid by Taxpayer Constituted Taxes Assessed Against Local Benefits.

In his argument, appellant overlooks the fact that a Reclamation District is a separate legal entity and a *quasi* public corporation, separate and apart from the land owners, even if all of the land in the district were owned by a single owner, which at the time of the formation of the district and the construction of the improvements in the district was not the situation here. [R. 134-138.]

At the time of the formation of the district and the approval of the plans by the Reclamation Board of the State of California, there were eight other land owners in the district, and the improvements were made entirely separate and apart by Mr. and Mrs. Birch and Mr. and Mrs. Conaway, as contractors, entirely separate and apart from the district. [Stipulation of Facts, R. 134-138.]

In 1920 the Commissioners of Assessment, duly appointed, assessed the value of the benefit to the lands in the district from the improvements contemplated and ap-

portioned the cost of such improvements according to the benefits that would accrue to each of the nine tracts of land then comprising the district. [R. 137.] The issuance of the bonds did not occur until five years later. [R. 139.]

Certainly when this assessment was made, the assessment was a bona fide assessment duly made and the Reclamation District was a bona fide district duly organized. Also, the bonds thereafter issued were duly issued and constituted a valid lien against the lands of the district. Under the laws of the State of California for such cases specially provided the Superior Court of Yolo County, so held. (Statement of the Case, *supra*, and Section 3478 of the California Political Code.)

There is no question here even of any intention of tax avoidance.

Mr. Birch testified as follows:

“Q. (By Mr. Acret): Mr. Birch, in participating as one of the landowners (170) in the formation of Reclamation District No. 2035, did you or your associates have any intention of tax avoidance?
A. No, it never occurred to us.

* * * * *

Q. Did you in any way have any intention of tax avoidance in connection with that matter? A. None whatever. (171.)

Q. How long was it that you waited for your money for the work that you and Mr. Conaway did in improving the district from the time of the commencement of the work until the time that you got the money or the bonds in payment therefor? A. About six or seven years. [R. 297.]

* * * * *

Q. Did you, yourself, receive any advice from any attorney or accountant with respect to the tax phrase of that matter, prior to the organization of any reclamation district? A. No, and, furthermore, we didn't have any thought in mind of ever getting out a bond issue.

Q. How did you learn of the tax exempt phase of that matter, if you can recall, back when it first came to your attention? That was a matter of State law, of course, but when did that first come to your attention? A. After we received the bonds in 1925.

Q. You did not know of it, then, before that time? A. No." [R. 337-338.]

Appellant overlooks the fact that in constructing and developing for the district 45 miles of roadways and 47 miles of irrigation canals and 55 miles of drainage canals and ditches, the landowners in the district constructed and developed rights of way and so forth which became a part of the Reclamation District and property rights entirely separate and apart from the lands owned by the various owners in the district, including the Conaway ranch.

In *Western Insurance Company v. Drainage District 72*, 72 Cal. App. 68, 72, it is held that though the administration of the affairs of reclamation districts is committed entirely to the owners of the lands embraced within the districts, that nevertheless such districts are "public mandatories and governmental agencies through which the state administers and executes one of its most important functions."

Appellant overlooks not only the record facts but also all the requirements and provisions of the Reclamation Act, to-wit, Section 3480 of the California Political Code, the applicable portions of which are set forth as Appendix B

to this brief. This Act provides for the manner of the formation of a reclamation district; the issuance of bonds; the validation of these bonds; the assessment of lands in the district to meet the expenses of the district, including payment of interest on these bonds; and for the payment of all moneys collected from such assessments *into the County Treasury*; for all unpaid installments of assessments to constitute a lien upon the lands in the district until paid, and permitting the land owners to pay the assessment installments, either in cash or with the interest coupons of the bonds.

The Reclamation District is a separate legal entity, and under the laws of the State of California, the County Treasurer in behalf of such separate entity was obliged to collect the principal and interest of the assessment against the taxpayer's lands and to maintain a lien against such lands until such principal and interest is paid and to foreclose such lien if and when the payment of such principal and interest is in default.

Regardless of all of the foregoing, as pointed out by the Tax Court's decision, the bona fide character of the bonds, the varied character of their ownership, and their having been extensively dealt in for value over a long period of years, is in itself alone a sufficient reason to remove all question of the payor and the payee on the bonds being economically identical, and to remove all question as to the right of the taxpayer to make the deduction involved herein.

Even if all of the lands in the district had been owned by the taxpayer, and the taxpayer had owned all, or most, of the bonds, nevertheless it would have been entitled to deduct the money it paid to the County Treasurer to meet

the interest accrued on the bonds. The provision for the issuance of bonds, the income from which was exempt from taxation, contemplated just such a situation and the possibility of the ownership of the bonds by the owner of the lands in the district. The purpose was to encourage, *and coerce*, reclamation of marginal and swamp lands in the state of California and to hold out the advantage of exempt bonds even if the taxpayer should own *all* of the lands in the district and *all* of the bonds, which however does not happen to be the situation of ownership in the instant case.

In the case of *Western Assur. Co. v. Drain Dist.*, 72 Cal. App. 68, 72, it is stated as follows:

“ . . . Some of the drainage and reclamation and irrigation districts considered by the cases just mentioned were formed and organized under special acts of the legislature and some under the general laws of the state, and, while the administration of the affairs of all of them is committed entirely to the owners of the lands embraced within the districts, still they are, nevertheless, public mandatories or governmental agencies through which the state administers and executes one of its most important functions. The reason that that is so as to reclamation districts is because the swamp and overflowed lands of California were granted by the general government to the state upon condition that the latter would see to the reclamation of the same so that they might become suitable for the purposes of cultivation, and, as an essential corollary of that proposition, those who purchase such lands from the state so take them subject to the right, and, indeed, the duty of the state, either by a scheme immediately directed and supervised by itself through officers or agents appointed for that purpose, or by committing that duty to the owners themselves of such

lands, to coerce such reclamation according to such rules, regulations, and plans as may be prescribed by the state through its legislature.” (Emphasis added.)

The provisions of the Reclamation Act itself disclose this intention. Section 3480 of the Political Code provides:

“Any landowner of the district *who shall desire at any time to lessen* or remove the lien upon his land of any assessment on which bonds have been or hereafter may be issued *may* deliver to the County Treasurer for cancellation any bonds payable out of said assessment, and the Treasurer shall credit against the assessment on his land the principal and accrued interest of said bonds.” (Emphasis added.)

Regardless of the ownership of the bonds, of the ownership of the lands, or the taxpayer's intentions, in order to avail itself of the express provisions of the laws of the State of California with respect to reclamation districts and reclamation bonds, it was entitled to deduct moneys paid to the County Treasurer to meet interest on the bonds and to treat as exempt such moneys when received back from the County Treasurer.

The foregoing constitutes obviously some of the reasons as to why from 1925 to 1934, while Mr. and Mrs. Birch owned all of the lands in the district except 240 acres, and while they owned a little more than half of the bonds, they were permitted by the Commissioner to deduct all of the money paid to the County Treasurer to enable the district to meet interest on all of the bonds, including the bonds owned by themselves, and at the same time they were not obliged to account to the government for this money as

income when it was paid back to them by the County Treasurer as interest from the bonds.

After the State of California holds out to its citizens the tax advantages resulting from the development of marginal and swamp lands and of the issuance of bonds to cover the cost of such development, in order to encourage such development, it would seem to be an act of bad faith for the government to attempt to deprive the taxpayer of such advantages.

From the foregoing it appears that respondents' reasons for the assessment not constituting an assessment for local benefits is fallacious, as well as being unsupported by the facts.

B. The \$221,610.87 Is Deductible Because It Is Not "Interest Paid" but "Taxes Paid" to Meet Interest Charges With Respect to Assessments Against Local Benefits.

The Tax Court in its opinion stated as follows:

"Principal and interest were payable out of moneys collected by the treasurer of Yolo County from assessments against the benefited lands, which assessments were to be deposited 'into the main county treasury,' but 'credited to the bond fund' of the District, as provided by Section 3480, Article II, c. 1, Title 8, Deering's Political Code of California. [R. 389-390.]"

From the said Section 3480 and from the argument under the preceding sub-heading, it would seem that the above-quoted statement is clearly correct. The Birches and the Conaways had a right to act, as contractors, in constructing the improvements upon the various rights of way of the District, the same as any other persons, and

they had a right to be paid for such work by the issuance of a warrant, and under the laws of the state to have bonds issued in payment of such warrant. After the bonds were issued, nearly half of them became owned by various third parties, and for over a period of more than twenty years such bonds as to their principal and interest, with one small exception, were dealt in upon the basis of their face or par value.

There is no similarity whatsoever in the facts in this case to the facts in any of the cases cited by petitioner.

As held in the case of Andrew Little, *supra*, the payment to the County to meet interest on such bonds constitutes a payment of taxes and not interest within the meaning of a similar section of the then existing Revenue Act.

During all of the period involved in this action, nearly half of the bonds were owned in arm's length transactions by third parties, and even if the bonds had all been owned by taxpayer, the payor and the payee were not economically identical. The intervening party was a bona fide reclamation district of the State of California, the financial agent of which was the County Treasurer of Yolo County, who was obliged to act under the provisions of said Section 3480 of the Political Code.

As argued under a previous point, the Reclamation Act itself contemplates that the landowner in the district may own the bonds. It provides that he *may* remove the lien of the bond upon his land if he "*shall desire*" by turning in the bonds *at any time* to the County Treasurer. There is no requirement in the Act that he shall turn in the bonds at any time.

As heretofore shown, the purpose of the provision that the income from reclamation district bonds shall be exempt from taxation was in order to encourage the development of marginal lands in California. It was in order to "coerce" the development of such lands. Also heretofore shown, the statute expressly provides that such bond issues may be refunded, and the refunding of such bond issues is a common practice in the State of California. As also heretofore shown, however, in the instant case the bond issue was refunded, and there was delay in providing the money to pay for some of the bond interest coupons, for the reason that the taxpayer had been connected with a bank which failed, and until 1944 it was without sufficient money.

C. The Taxpayer's Deduction of the Payment of \$221,610.87 as Taxes Is Not in Conflict With the Purpose of Section 122(d)(2) for the Reason That Such Payment Was for Taxes Actually Due and Payable, and Which in Fact Did Constitute an Economic Loss.

The argument under this point is covered not only by the facts of the case as heretofore stated, but by the statements contained under previous points.

If the taxpayer had not met the call of the County Treasurer to enable him to pay the matured interest coupons upon the bonds owned by the Hopkins, Miss Minter, and the Republic Life, which constituted close to one-half of the entire bond issue, such owners would have caused the entire bond issue to be foreclosed. As to the payment of the calls to meet the interest accruing on these bonds, and as to the taxpayer's purchase of matured in-

terest coupons of these bonds, it suffered an economic loss. As to the taxpayer's payment of that portion of the call which related to an amount of money sufficient to pay the interest coupons owned by the Birch Securities Company, the taxpayer in fact also suffered an actual economic loss in view of the intervention of the County Treasurer. Under the provisions of the statute all of the money so paid went into the general fund of the County Treasury and the County Treasurer was obliged to pay it out to any holder of interest coupons whomever he might be.

As stated by the Tax Court:

"The funds which the district collected by its assessment calls were for the payment of interest in general, and we are of opinion that petitioner's right to deduct its payments as a tax is not defeated by the fact that a part of such payments became available to pay interest on bonds held by it, by Securities, by Holding, or by the Birches. Andrew Little, 21 B. T. A. 911.

"Respondent argues further that the 'payments of interest on reclamation bonds' was the payment of interest on indebtedness incurred and continued to purchase and carry tax-exempt obligations, and hence such payments are not deductible under section 23(b), Internal Revenue Code. Recognizing the reclamation district as a legal entity, we view petitioner's payments as made in satisfaction of taxes, not of interest, and the argument thus lacks factual foundation. As taxes assessed for interest only, they are not of a kind tending to increase the value of the property assessed, and are hence properly deductible. Mary E. Evans, 42 B. T. A. 246; Missouri State Life Insurance Co., 29 B. T. A. 401; Andrew Little, *supra*."

POINT TWO.

The Reclamation District Being Regularly Formed by a Group of Eight Property Owners in Addition to the Birches, and the Bonds Having Been Regularly Issued to Pay for Improvements of a Bona Fide Value in Excess of \$2,000,000, Such District and Such Bonds Did Not Lose Their Bona Fide Character by Reason of the Subsequent Acquisition by Respondent Corporation, as the Birches' Successor in Interest, of Practically All of the Land in the District and a Substantial Portion of the Bonds.

It would seem that the correctness of the above statement would be obvious.

To take a somewhat similar illustration, if the Birches had owned lots in two city blocks and had caused the city, in a street proceeding, to pave the street running between those two blocks and to assess the cost thereof against the lots in each of the blocks, and had caused ten-year bonds to be issued against the two blocks in the district, surely it would not be contended that the street improvement district and the bonds had become identical because of the Birches' subsequent acquisition of all but one of the lots and more than one-half of the bonds. Nor could it be so contended even if the Birches had acquired all of the lots and all of the bonds.

POINT THREE.

Where Respondent's Predecessor in Interest, Mr. Birch, Was Nearly Seventy Years Old and During the Depression Could Not Get Bank Credit Sufficient to Enable Him to Operate the Ranch Unless He Placed the Title Thereof in a Corporation, and Where the Taxpayer Corporation Was Formed for the Purpose of Securing Such Bank Credit, There Is No Question of Alter Ego, and the Corporation Is an Entirely Separate Legal Entity With Respect to Taxation, as Well as in Every Other Respect.

It is immaterial as to whether the Birch Securities Company, which owned the bonds, was the *alter ego* of the Birches. It is sufficient that respondent, the Birch Ranch and Oil Company, is a separate legal entity.

As heretofore shown the parties stipulated as follows:

"17. On October 15, 1934, Birch and his wife organized Birch Ranch and Oil Company, the petitioner herein, and transferred to it the Conaway Ranch, their interest in the Birch Oil Company, the partnership which succeeded the Menges Oil Company in 1911, and all other property belonging to them, except the bonds of Reclamation District No. 2035, certain corporate stock and other properties having a value of about \$600,000. Birch had been having difficulties during the depression years in borrowing on his personal credit the moneys needed for the operation of the ranch, and the petitioner was organized for the purpose of procuring needed bank credit."

It would seem that there could be no possibility of respondent being the mere business conduit and *alter ego* for the Birches. At the time they formed the company, they merely turned over to it the title to the lands comprising the Conaway ranch. They held out, and kept in their own names, the title to properties having a value of about \$600,000 [R. 143] and this property never did go into the corporation. "Birch had been having difficulty during the depression years in borrowing on his personal credit the moneys needed for the operation of the ranch, and (the taxpayer) was organized *for the purpose of procuring needed bank credit.*"

It would be difficult to conceive of a corporation being organized in a manner sufficient to constitute a separate legal entity under more compelling facts and circumstances.

The very purpose of a corporation is to enable it to enjoy credit separate and apart from the risk of the personal indebtedness of its shareholders, with respect to taxes, as well as in every other respect. Certainly, business houses and banks ought to be free to extend credit to such a corporation without the corporation becoming liable, or mixed up in any respect whatsoever, with the personal indebtedness of the Birches, or any of their other companies, with respect to taxes or any other indebtedness. If this were not so, corporate credit, and the backbone of free enterprise in America, could not exist.

This point, though quite unnecessary, would seem to be compelling.

Conclusion.

It would seem that the decision of the Tax Court ought to be upheld and the petition herein denied.

Respectfully submitted,

GEORGE ACRET,

Attorney for Respondent.

APPENDIX A.

BOND OF RECLAMATION DISTRICT 2035

United States of America

State of California

County of Yolo

Number

2000

Dollars

1000

Reclamation District

No. 2035

Reclamation District No. 2035 for value received hereby acknowledges itself indebted to and promises to pay to the holder hereof at the office of the treasurer of said County in State of California, on the first day of January, 1943 the sum of

One Thousand Dollars (\$1000.00)

in gold coin of the United States of America, with interest thereon in like gold coin from date hereof until paid, at the rate of six per cent. per annum, payable at the office of said treasurer semi-annually on the first day of January and the first day of July in each year on presentation and surrender of the interest coupons hereto attached. This bond is one of a series of 2265 bonds of like tenor and effect as to denomination and maturity, numbered from 1 to 2265, inclusive, amounting in the aggregate to Two million two hundred sixty-four thousand seven hundred forty Dollars (\$2,264,740) issued in accordance with section 3480 of the Political Code of the State of California pursuant to an [235] election held in said

Reclamation District on the 28th day of August, 1924, authorizing its issuance, and is based upon and secured by an assessment levied on the lands in said district, and filed in the office of the county treasurer of said County of Yolo on the 23rd day of July, 1924, and the said Reclamation District does hereby certify and declare that said election was duly called and held upon due notice, and the result thereof was duly canvassed and ascertained in pursuance of and in strict conformity with the laws of the State of California applicable thereto, and that all of the acts and conditions and things required by law to be done, precedent to and in the issue of said bonds have been done and have been performed in regular and in due form and in strict accordance with the provisions of the law authorizing the issuance of reclamation bonds.

In Testimony Whereof, the said District, by its board of trustees, has caused this bond to be signed by the president of said board and attested by the auditor of said County of Yolo, with his seal of office affixed this 1st day of January, 1925.

C. HAROLD HOPKINS
President of said Board

Attest:
[Seal]

P. D. WALLACE
Auditor of the County of Yolo
State of California [236]

APPENDIX B.

EXCERPTS FROM SECTION 3480 OF THE CALIFORNIA
POLITICAL CODE, WITH APPROPRIATE EMPHASIS
ADDED:

Action to test legality. At any time within thirty days after said bonds shall have been delivered to the treasurer of the county, an action may be commenced in the superior court of said main county by the trustees of said reclamation district in its name against the lands in said district and all persons owning the same or interested therein, to have it determined that said bonds are a legal obligation of such reclamation district, and in the event no such action is brought then the same may be commenced by any land owner in the district within thirty days thereafter. It shall be sufficient to describe said lands as all lands in the district (naming it), without a more specific description. The summons shall be published once a week for two weeks in some newspaper of general circulation published in the county where the action is pending. Within thirty days after the first publication of summons any owners of land in such district, or any person interested, may appear and answer the complaint, which answer shall set forth the facts relied upon to show the invalidity of said bonds. The default of all defendants not so appearing may be entered. Such action shall be given precedence in hearing and trial over all other civil actions in such court, and judgment rendered declaring such matter so contested either valid or invalid. Any party not in default may have the right to appeal to the Supreme Court within thirty days after the entry of judgment. Judgment for the plaintiff in such proceedings shall be considered as a judgment *in rem* and shall be conclusive against said

district and against all lands therein and all owners thereof and other interested persons.

* * * * *

Bond fund. All moneys collected by any county treasurer upon any assessment upon which bonds shall have been issued, including all moneys derived from sale of land for delinquent installments, or from redemption thereof, or from sale of lands bought by the treasurer at any such sale, *shall be by such treasurer forthwith paid into the main county treasury* and except as otherwise provided in section 3466a of this code, shall be credited to the bond fund of such reclamation district and used exclusively for the payment of principal and interest of said bonds issued on such assessment, and of the principal and interest of any refunding bonds issued thereon, and the expenses of the county treasurer as hereinafter provided.

* * * * *

Additional assessment. The lien of any unpaid assessment upon which bonds shall have been issued shall continue until all said bonds, and any refunding bonds which may be issued, shall have been paid in full except as hereinafter provided in reference to the use of bonds as payment of assessments, and if for any reason any part of such principal or interest of said bonds, or of refunding bonds shall remain unpaid after enforcement of said assessment as in this article provided, the board of supervisors of the main county shall order an additional or supplemental assessment to be made as provided in section 3459, sufficient to pay such unpaid principal and interest; which additional or supplemental assessment shall be enforced and collected in the same manner as the original assessment.

Interest on unpaid installments. Where bonds of the district have been authorized to be issued on such assessments all unpaid assessments shall bear interest at the rate of seven per cent per annum from the date of the bonds originally issued thereon until such bonds and any refunding bonds issued thereon shall have been fully paid and discharged, and the interest due at any time on said unpaid assessments may be called without calling any installment of the said assessment. The word installment as used in this section shall be construed as applying to interest as well as the principal as the case may be.

Estimate of assessment installment to pay interest and principal. At least ninety days before any interest date of the bonds, including refunding bonds, *the county treasurer of the main county shall estimate the amount of money necessary to pay interest and principal maturing on such interest date after crediting thereon the funds in the treasury applicable to the payment thereof*, and the expenses of the county treasurer hereinafter provided and shall add thereto fifteen per cent of such aggregate sum to cover possible delinquencies, and said county treasurer shall thereupon cause to be published two times, to wit: once a week for two weeks in some newspaper of general circulation published in each county in which any of the district may be situate a notice substantially in the following form: (Name of reclamation district.)

Form of notice. Notice is hereby given that *an installment of assessment* (describing it) of \$....., beingper cent is payable within thirty days from (date) *by all assessed landowners* of said district in the county of (name of county) to the treasurer of said county. *All or any part of said installment which shall remain unpaid*

on the day (day fixed) will be delinquent, together with ten per cent of such installment added as penalty.

Dated (date).

(Signed).....,
Treasurer of.....County.

If no newspaper is published in said county, such publication shall be made in a newspaper published in an adjoining county.

Payment of installments: Delinquencies. Said installment may be paid either in cash or in bonds of said district, or their interest coupons, issued upon said assessment, then matured or to mature within ninety days from the date of the calling of such installment, taken at their face value, or part in cash and part in such bonds and/or coupons. Any bond or coupon so received in payment shall be by the treasurer forthwith canceled and filed in his office. If any part of such installment or any interest thereon shall remain unpaid at the expiration of thirty days from the date of said notice, it shall become delinquent and ten per cent of the unpaid amount of said installment shall be added thereto and collected by said treasurer.

* * * * *

Sale for delinquent installments. At the time stated in said notice, or such other time to which said sale may have been postponed, the county treasurer shall sell each parcel of land described in said notice to the highest bidder, unless prior thereto he shall have received payment in full of said delinquent installment together with such penalty.

* * * * *

Bonds as payment on assessment. Any landowner of the district who shall desire at any time to lessen or remove the lien upon his land of any assessment on which bonds have been or hereafter may be issued may deliver to the county treasurer for cancellation any bonds payable out of said assesment, and the treasurer shall credit against the assessment on his land the principal and accrued interest of said bonds.